

Performance as at 31 December 2023

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a. ¹
Fund ²	12.7%	16.0%	25.7%	17.9%	18.3%	14.6%
Benchmark ³	7.2%	8.5%	7.8%	0.9%	6.4%	6.2%
Difference	5.4%	7.5%	17.9%	17.0%	11.9%	8.4%
Microcap Index ^a	6.5%	5.3%	-0.4%	3.5%	13.1%	8.8%

¹ Inception date is 16 May 2016. Past performance is not a reliable indicator of future performance. All p.a. returns are annualised.

² Sphera Australian Microcap Fund. Returns of the Fund are net of applicable fees, costs, and taxes.

³ Benchmark is the S&P/ASX Small Ordinaries Accumulation Index.

^a Microcap Index refers to S&P/ASX Emerging Companies Accumulation Index.



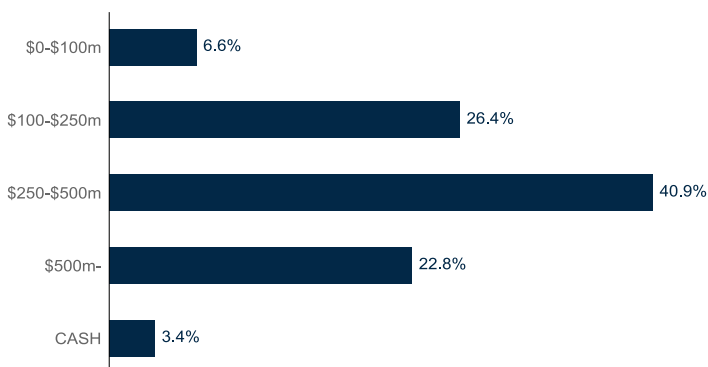
Overall Commentary

The Fund returned 12.7% (after fees) for the month of December, outperforming the S&P-ASX Small Ordinaries Accumulation Index by 5.4%.

Top 5 Holdings

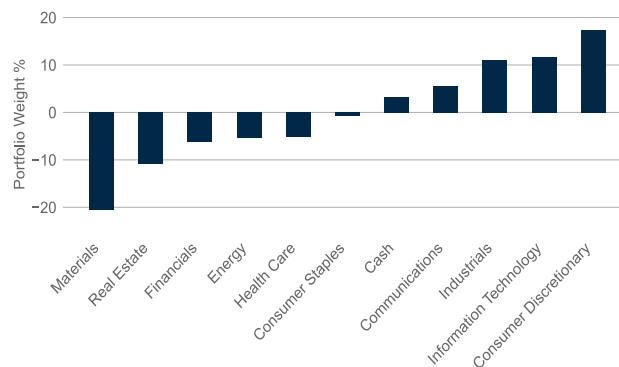
Company Name	% Portfolio
Adore Beauty Group Ltd	5.0
Vista Group International Limited	4.7
Articore Group Limited	4.6
GWA Group Limited	4.6
Supply Network Limited	4.5
Top 5	23.4

Market Cap Bands



Source: Sphera Asset Management

Active Sector Exposure



Source: Sphera Asset Management

Markets

December was an extraordinary month for the Fund. With corporate activity having taken a bit of a backward stance during the latter part of the year, it came back with a vengeance in December. Two of the Fund's holdings (A2B Ltd (A2B.ASX) and Pacific Smiles (PSQ.ASX)) received firm bids during the month. What drove this appears to have been the confluence of several factors – firstly valuations were low in all of the names attracting bids, secondly there is now a building consensus that interest rates are likely to have peaked in the US and not far off their peak in Australia. We support this view on the basis that the remarkable events around Covid ended up being a co-ordinated super inflationary event which has since been unwound. The monetary tightening globally, higher interest rates and the re-opening of economies has seen a lot of excess liquidity drained from global economies and production bottlenecks unwind. Supply chains have largely normalised. In China we are seeing deflation – yes you read that correctly – deflation with consumer prices down 0.5% YoY and producer prices (the prices manufacturers broadly charge for goods) down 3% YoY.

Consumers are struggling in Australia with retailers reporting very tough trading environments, however, housing prices remain strong and unemployment relatively low. These are confusing signals for the RBA to interpret. Nonetheless we would expect an easing bias late in 2024 assuming domestic inflation rates continue to be downward trending – which we think likely. This backdrop should be relatively kind to small cap investors. Small caps have materially lagged large caps over the past two years (smalls[^] have underperformed by 14% and micros[^] by 27% vs. the ASX 100 to 31 December 2023). The December rally in small caps was mirrored by large caps meaning the underlying performance gap still remains. If the interest rate environment continues to ease, we would suspect a relatively supportive environment for small and micro caps over the next year.

Major Contributors to Performance

Over the month the largest contributors to performance were from overweight positions in Articore Group (ATG.ASX, +59%), Pacific Smiles (PSQ.ASX, +34%), and Vista Group International (VGL.ASX, +30%).

Articore Group (previously named Redbubble) (ATG.ASX) share price rose 59% in December on no new company specific news. The rally feels like a reprieve after the share price sold off in the months prior. In October the business revealed the company had returned to positive underlying cash flow after what has been a volatile trading environment for the retail business. The co-founder returned early in the year and has been focused on cutting costs and improving cashflow, as it returns to a more normal operating environment post COVID. We believe the business is taking the right steps to realign the cost base. The business operates leading global online marketplaces, Redbubble and TeePublic and generates \$450m of revenue with a strong balance sheet. Assuming the company can return to modest mid-single digit operating margins the business trades on 5-6x EV/EBIT.

Pacific Smiles (PSQ.ASX) share price rose 34% in December after a share market raid/non-binding proposal from Genesis Capital Manager to acquire the group at a share price of \$1.40, which we sold into. This represented a significant return in a very short period for us given we opportunistically acquired a substantial shareholding (average entry price <\$1) when several large sellers aggressively exited the stock in November/December at pretty much all-time lows. PSQ's share price had fallen significantly over the last few years as the company generated negative operating leverage not helped by slower than expected normalisation of dental visits and high cancellations post COVID combined with weaker economic conditions and inflationary pressures, particularly around labour which is one of their largest costs. The share price weakness provided an opportunity to enter the name on valuation grounds premised on a return to a more "normal" macro environment in the medium to long term which would drive better utilisation in clinics and thus positive operating leverage.

Major Detractors from Performance

The largest detractors from performance included **not owning** Neuren Pharmaceuticals (NEU.ASX, +61%), and overweight positions in Praemium (PPS.ASX, -7%), and Mader Group (MAD.ASX, 0%).

Neuren Pharmaceuticals (NEU.ASX) share price rose 61% in December, however we did not own the company and hence it was a detractor from performance. Neuren is a biopharmaceutical company that is developing new drug therapies to treat highly debilitating neurodevelopment disorders that emerge in early childhood, with their approved drug trofinetide (sold under "Daybue") treating Retts syndrome. The strong share price performance over the month comes as the company announced positive results from its Phase 2 trial

of Phelan-McDermid syndrome (rare genetic condition that causes developmental and speech delays, behavioural problems and a weakening/no ability to feel pain or sweat).

Praemium (PPS.ASX) share price fell 7% in December on no new company specific news but underperformed the market which rose over the month. In late November the company provided guidance at their AGM, stating EBITDA would be ~20% lower than pcg which was below consensus and our expectations. The downgrade was driven by a combination of increased costs (+10% on prior half) and pressure on the revenue margin. The announcement came as a shock to the market and the stock was sold off aggressively on the back of this. Whilst disappointing, the business is the 3rd specialty financial platform behind HUB.ASX and NWL.ASX but trades on ~1/3 of the EBIT multiple at around 12x FY 24 EV/EBIT. We have added to the position on the pull back.

Outlook & Strategy Going Forward

Fairly evidently, we are constructive on smaller companies in 2024. Whilst it's true that – to paraphrase Buffett – you should never ask a small-cap manager if its time to buy small caps* – we still think it's about the right time to buy small caps. Just as many investors have moved capital into the relative safety of larger liquid and less economically sensitive names during a downturn, so too will they likely return to the smaller end of the market to increase returns when rates and confidence turns. We would also like to note, with sadness and gratitude the passing of Charlie Munger who died in late November just shy of his 100th birthday. Charlie was the slightly lesser known of the Buffett/ Munger duo but undoubtedly an equal intellectual contributor to the investment advice and wisdom that has emanated forth from Berkshire Hathaway. Many of our investment team were drawn to investing after reading some of the intelligent and humorous advice from Buffett and Munger. We are grateful for his intellectual curiosity, humility and generosity of spirit in sharing his wisdom and life outlook with us. Thank-you Charlie.

*Buffett quips that you should never ask a barber if its time for a haircut because the answer is always “yes”.

^Smalls = S&P-ASX Small Ordinaries Accumulation Index & Micros = S&P/ASX Emerging Companies Index

Platform Availability List

The Sphera Australian Microcap Fund is available on the below platforms. Platforms provide investors with consolidated and centralised reporting (including administration, tax, and distribution) by bundling together a range of managed funds as one single product

Acclaim Wealth	HUB24	MLC Navigator	Praemium
Asgard	Insignia Expand	MLC Wrap	Premium Choice
BT Panorama	IOOF Portfolio Service	Netwealth	
DASH	Macquarie Wrap	OneVue	
DPM	mFund	PowerWrap (IDPS only)	

Sphera Australian Microcap Fund	
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Investment Objective	The Funds aims to outperform the S&P/ASX Small Ordinaries Accumulation Index over the medium to long term
Investing Universe	Primarily listed companies outside the top ASX 250 listed companies by market capitalisation and companies listed on the New Zealand Stock Exchange with an equivalent market capitalisation
Holdings	Generally 20-65 stocks
Distributions	Annually
Fees	1.35% p.a management fee & 20% performance fee of the Fund's excess return versus its benchmark, net of the management fee
Cash	Up to 20% cash, typically 5% - 10%
Expected Turnover	20% - 40%
Style	Long only
APIR	WHT0066AU
Minimum Initial Investment	\$25,000

Fund Ratings



Contact Us

For more information, please contact Pinnacle Investment Management Limited on 1300 010 311 or email distribution@pinnacleinvestment.com

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Link to the [Product Disclosure Statement](#)

Link to the [Target Market Determination](#)

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